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BY HAND

Mary L. Cottrell, Secretary
Department of Telecommunications and Energy
One South Station, 2nd Floor
Boston, MA 02110

Re: Risk-Management NOI – DTE 01-100

Dear Secretary Cottrell:

Blackstone Gas Company ("Blackstone" or the "Company") provides the following comments concerning the Risk-Management Notice of Inquiry ("Risk-Management NOI") issued by the Department of Telecommunications and Energy ("Department") on December 4, 2001.

The Company is a small local gas distribution company serving less than 1,100 customers including more than 900 residential customers. The Company issued a Request for Proposals and obtained a contract with a third-party supplier to manage its transportation assets and provide gas sales for its base load and peak gas requirements. This contract was approved in *Blackstone Gas Company*, DTE 01-71. The contract has a current term which expires on October 31, 2005.

Based on current Department policy the contract provides for gas to be priced at various market-based indices. The Company does have an option to purchase its peak winter gas, in excess of its daily base load gas, either at a fixed-price or at a market index for Zone 6. The Company must make an election to choose the fixed-price option by July 1 of each year. The default price is the market-based index price. To date the Company has not elected the fixed price option for peak gas supplies. The Company does not plan to make such an election unless directed to do so by the Department, in that case all gas costs from such election should be recoverable by the Company.

If the Company had elected the fixed price option for the 2000-2001 winter, peak gas costs would have been lower than actual. However, if the Company had elected the fixed price-option for the current winter, it appears that the peak gas costs will be more than under the market-index based on the current and projected gas prices. Thus, while a fixed-price can increase price stability, it does not necessarily mean the lowest price for retail customers.

Under its current cost of gas adjustment clause ("CGAC"), the Company normally files a fixed-price gas charge for the entire winter period in September. Only when gas prices rise or fall significantly from original market projections does the Company file to request an interim increase or decrease in the gas charge. Last year the Company filed for and was granted an increase because of changes in the world gas markets. This year the Company filed for and was granted a decrease in its gas charge even after the transfer of certain gas related working capital and bad debt expenses from base rates. See, *Blackstone Gas Company*, DTE 01-50 (November 28, 2001 and Compliance Filing of December 19, 2001).

The only type of risk-management that seems appropriate for the Company to consider is a fixed price contract for all or a portion of its gas supply. However, as noted above, there is no assurance that any fixed price obtained by the Company will be lower than an indexed-price. In fact, because of the small quantities purchased by the Company, and its limited bargaining position, total gas costs could be more expensive. Blackstone cannot take the risk of providing customers with lower gas costs from a fixed price contract when the fixed price is lower than the index price and be required to bear the higher gas costs when a fixed price contract is higher than the index price. All costs for gas supply must be fully recoverable by the Company provided the Department initially approves the gas supply contract. See *Blackstone Gas Company*, DTE 01-71. Thus, Blackstone urges the Department to make any risk-management program voluntary and to allow for full cost recovery of all gas costs including risk-management costs incurred by the Company.

Blackstone provides its responses to the questions propounded in the Request for Comments by the Department, as follows:

Question 1. Should Massachusetts gas utilities be allowed or required to implement a risk-management program to mitigate price volatility for gas customers?

Response: Massachusetts gas utilities should not be required to implement a risk-management program. Any such program should be voluntary. For a small LDC like Blackstone Gas Company, serving less than 1,100 customers, the cost of implementation of a risk-management program could exceed any potential customers benefits.

Question 2. How will risk-management by LDCs affect gas unbundling and customer choice in Massachusetts?

Response: If risk-management programs provide customers with a fixed price option as an alternative to regular default service, this offering could be competitive with a fixed-price product offered by competitive suppliers and thus may retard the development of third-party competitive gas sales.

Question 3. Should gas utilities be limited to specific types of risk-management instruments? If so, what types?

Response: No. Any program of risk-management should be flexible and the LDCs should be allowed to select any reasonable risk-management instrument.

Question 4. Should there be a percentage volume of gas that LDCs would be allowed to hedge?

Response: No. LDCs should be allowed, but not required, to hedge a portion or all of their gas volumes.

Question 5. What should the core objectives of a hedging program be (e.g., least cost, price stability)?

Response: Price stability should be the core objective of any hedging program.

Question 6. How will the Department assess risk-management programs? What benchmarks should be used to measure a risk-management program's performance?

Response: Risk-management programs proposed by an LDC should be pre-approved by the Department, if consistent with the public interest. The Department should not second-guess programs based on a comparison of hedged prices to actual market prices.

Question 7. What standard of review should the Department apply to the utilities' initial risk-management program?

Response: Any program of risk-management should be voluntary and be subject to pre-approval by the Department. The standard applicable to a risk-management program proposal for pre-approval should be that the proposal is "consistent with the public interest."

Question 8. What types of costs are associated with risk-management? Should LDCs be allowed to recover these costs? If so, please explain how.

Response: All costs incurred by an LDC in connection with a risk-management program should be recoverable. An LDC should estimate its costs for the risk-management program and add them to the fixed-price option offered to customers. These costs should be reconciled in a subsequent period based on actual costs and sales under this option. In the alternative, these costs could be recoverable as part of the CGAC reconciliation process.

Question 9. Should an incentive mechanism be used in conjunction with a risk-management program? If so, please explain how this mechanism should be structured.

Response: An incentive mechanism should be a voluntary provision in any risk-management plan to be reviewed and approved by the Department, if appropriate.

If you have any questions concerning these comments, please contact the undersigned.

Very truly yours,

Andrew J. Newman
Attorney for Blackstone Gas Company

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cc: William H. Stevens, Jr., Hearing Officer
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